F1F!NINTH CIRCUIT PUTS THE KIBOSH ON COMMON FUND CLASS ACTION SETTLEMENTS

Federal Court of Appeals Rules That Common Fund Settlements Must Have Driving Nexus to Injured Class Members, Calling Into Question Future Class Action Settlements

Class Actions are the bane of corporate America. When the corporation stubs its toe, a greedy class action lawyer seizes the opportunity to sue for millions, To buy peace, the corporations often throw in a few million (from insurance) to make the case go away. But what happens to the money? Sure, the class action lawyer gets rich, and the class receives a pittance, what happens to the rest? Like nobility traversing through Sherwood Forest, the corporation agrees to settle with Robin Hood to fund specified charities for its sins.

Most cases are settled on a "common fund" basis where the corporation distributes a pile of money, and the class members get a stupid coupon or a $5 check, the class action lawyers get a huge sum, and the rest is given to charity to feed the homeless or save the whales. A class action administrator charges $100-300,000 to administer the whole process.

The common fund has to be extraordinarily large because at least in Federal Court, attorney fees are a percentage of the common fund, usually around 25%. So if the class action lawyer is going to get a nice paycheck, say in the neighborhood of $250,000, the common fund has to be at least a million dollars.

A common fund settlement which gets distributed in this fashion is often called a "*cy pres*" settlement, which is Latin for ""as near as possible." In short, not all the money can realistically go to the class members for their $5 purchase or to the lawyers, so the Court approves a give-a-way to charities. It makes corporate American feel good, corporate America pays the ransom, the class action lawyers get a nice pot, and some deserving charities get large contributions. Sounds great, doesn't it?

But recently, the Ninth Circuit put its foot down and put the kibosh on these Robin Hood class action settlements in the case of Dennis v Kellogg Co., 2012 WL

2870128 (9th Cir. 2012). The case is significant, because unless the lawyers get really creative, this may spell the end of for this type of class action settlement.

Some background on the case is necessary. Kelloggs markets cereals like “Frosted Mini-Wheats” claiming that it is “part of a nutritious breakfast” and “helps improve children's attentiveness by nearly 20%.” As ridiculous as that advertising slogan was, the fact that a class action lawyer sued to stop the practice was equally ridiculous. Kelloggs quickly bought their peace, and agreed to a $2.75 million dollar “common fund” settlement, whereby purchasers of the product would receive $5 per box of cereal purchased, up to a maximum of $15. The rest of the money would go to charities selected by the parties, and Kelloggs would also donate $5.5 million worth of specific Kellogg food items to charities that feed the indigent. Kelloggs agreed to pay the class action lawyers a sum not to exceed $2 million. The total value of the settlement was nearly $10 million dollars.

The parties brought the case for approval of the settlement, and the trial court approved the settlement. In a surprise decision, the Ninth Circuit disallowed the settlement, sending the case back to trial court.

The basis of the ruling is that the *cy pres* charities have to have a “driving nexus” to the injured class. So if the class consists of children who ate Frosted Mini-Wheats and didn’t have 20% more attentiveness, then the charity has to relate geographically and functionally to inattentive children. Feeding indigent children through a variety of charities was neither functionally nor geographically related to inattentive children in America.

The Court summed everything up in the final paragraph when it stated:

> Class counsel and Kellogg ask us for the impossible. …The settlement provides no assurance that the charities to whom the money and food will be distributed will bear any nexus to the plaintiff class or to their false advertising claims and therefore violates our well-established standards governing *cy pres* awards. Moreover, the attorneys' fees are impermissibly high considering what the defective settlement provides the class.

Accordingly, the Ninth Circuit sent the case back to the trial court. This was one instance where the typical Robin Hood class action settlement wasn't going pass the muster.

The Dennis case is a double edged sword for class actions. On the one hand, insurers for corporate America simply want to write a check and get out of expensive class action litigation. So this may force up defense costs if the case can't settle. On the other hand, if no such Robin Hood settlements were available to increase the pot size, the numbers of class action suits might decrease.

There are tangible lessons to be learned from the Dennis v Kelloggs case.

First, settlement judges and class action counsel will certainly have go to settlements more prepared with specific organized groups which address the harm suffered by the class, if they can be located.

Second, given the ticky-tack nature of some class action lawsuits, I find that it might be impossible to locate a charity sufficiently connected to the specific harm alleged to satisfy the Ninth Circuit.

Third, the settlement might have a provision for reversion of the funds back to the corporation or its insurers, or escheating the money to the U.S. Federal Government.

Finally, no matter how prepared counsel might be, there is no getting around that Dennis v Kellogg represents a reversal of the class action settlement engine, which might be a benefit to most corporations and their insurers. The trip through Sherwood Forest may not be as expensive as it once was.